FLEXI**PORTFOLIO**

PERFORMANCE REPORT

1 OCTOBER 2017

SOUTH AFRICAN ECONOMIC REVIEW

While August was a generally good month for South Africa, characterised by a firming rand and an unexpectedly strong second quarter GDP report, the tide turned quite dramatically in September as concerns over the economy, labour market, the fiscal situation and ratings mounted anew.

On the real economy front (that part of the economy dealing with producing goods and services), early data for the third quarter points to a renewed slowdown after the surprise 2.5% annualised expansion in GDP in the second quarter. While the news was not universally bad, the renewed slowdown highlights the fact that the economy still faces considerable cyclical and structural headwinds –with more tax hikes looming too, as the fiscal situation remains precarious. While we have kept our full-year GDP forecast of 0.8% unchanged, it is hard to see any meaningful improvement any time soon.

The consequence of the slow growing economy is that it is unable to cope with the growing labour force, reflected in the fact that in the year to June only about half of the 1.1 million people that joined the labour force actually managed to find some kind of a job. This resulted in the unemployment rate rising by a full one percentage point to a record 27.7% in the second quarter. Another implication of low growth is that we are falling off global investors' radar screens. This is starkly highlighted in the heavy selling by foreigners of local listed equities since last year. After selling R125 billion of equities in 2016, so far this year selling totals R91 billion. This compares poorly with the R66 billion of sales in 2008 at a time when emerging markets, in general, suffered heavy selling as the global financial crisis erupted.

Data released during September highlighted how precarious the fiscal situation is, owing to the weak economy. Over the first five months of the 2017/18 fiscal year, tax revenues rose by only 3% against a budget target of 9% – an undershoot against budget of about R20 billion for this period alone. It is difficult to see this situation improving sufficiently over the remainder of the fiscal year in order to meet the fiscal targets. In fact, concerns are that it may deteriorate further as corporate profits remain under pressure, subdued imports are depressing VAT on imported goods and wage settlements are decelerating, causing under-recoveries against budget on personal income taxes. It therefore seems that the budget deficit target for the full fiscal year of 3.1% of GDP could be missed by a wide margin of 0.5% of GDP, or even more. Such an outcome will not only pressure National Treasury to raise taxes considerably, piling more pressure on the economy, but also increases the risk of more downgrades to our ratings, with the investment grade on local government bonds particularly at risk.

With concerns mounting over the economy and ratings, and foreigners selling their locally held shares, the rand weakened notably from around R13.00 to the US dollar at the end of August to R13.60/US$ by the end of September. The weakening rand prompted the South African Reserve Bank to, against expectations of a cut, keep the repo rate unchanged at its mid-month meeting.

With the economy, the fiscal situation, consumers and businesses all under considerable pressure, the next few months will be difficult and can potentially see more pressure on the rand as three key events will take place in the final quarter of the year – namely the Medium Term Budget late in October, ratings reviews by Moody's and S&P late in November and the ANC's elective conference in December.

One can only hope that 2018 brings less political uncertainty, faster progress on confidence- and growth-enhancing economic policy reforms and a faster cyclical economic recovery. If not, the pressures on the rand and the economy will not ease.

MARKET PERFORMANCE INCLUDING DIVIDENDS

	LAST MONTH (%)	YEAR TO DATE (%)	1 YEAR (% P.A.)	3 YEARS (% P.A.)	5 YEARS (% P.A.)	8 YEARS (% P.A.)	10 YEARS (% P.A.)
JSE All Share	-0.9	12.6	10.2	7.2	12.5	13.8	9.5
JSE Fin & Ind	-0.8	12.7	10.1	9.9	16.4	18.4	14.2
JSE Resources	-1.1	12.4	11.1	-8.4	-2.5	0.5	-2.2
ALSI 40	-0.4	15.3	11.9	6.9	12.6	13.6	9.2
All Bond	1.1	7.8	8.2	7.6	6.3	8.7	8.4
Cash	0.6	5.7	7.6	7.0	6.4	6.3	7.2

RETIREMENT ANNUITIES TO 01/10/2017 (REFER NOTES)

	PERFORMANCE PROFITS									SMOOTHED BONUS			STABLE FUND			CPI
	Equity %			Balanced %			Select %			%			%			
Period	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	%
1 Year	9.2	4.0	4.0	8.9	5.4	5.4	8.6	3.8	3.8	7.6	7.7	7.7	6.4	6.4	6.4	4.8
2 Years	5.3	5.4	6.1	6.3	6.3	6.7	5.1	4.7	5.1	8.0	8.3	8.5	6.3	6.2	6.1	5.3
3 Years	4.6	5.4	5.3	6.1	6.5	6.6	4.6	5.5	6.3	8.7	9.0	9.7	6.1	6.0	5.7	5.1
5 Years	7.4	8.6	11.8	8.0	8.7	10.8	7.0	7.9	10.4	10.4	10.8	12.0	5.5	5.4	4.9	5.6
8 Years	10.3	10.8	11.7	9.8	10.0	10.5	9.2	9.6	10.0	11.1	11.1	10.9	5.0	5.0	4.8	5.2
10 Years	10.4	10.1	7.3	9.7	9.5	7.9	9.3	9.1	7.3	10.8	10.8	10.2	5.1	5.2	5.5	6.0
15 Years	11.7	11.7	12.8	10.5	10.5	11.2	10.5	10.7	11.7	11.5	11.5	11.5	5.4	5.4	5.7	5.8
20 Years	11.9	12.1	11.3	10.6	10.8	10.3	-	-	-	11.3	11.2	10.8	5.6	5.7	6.3	6.2
25 Years	12.0	12.2	13.1	10.8	10.9	11.7	-	-	-	11.3	11.4	11.8	6.5	6.6	7.8	6.7
INTERIM RATES										9.50% p.a. (0.759% p.m.)			0.513% p.m.			

ENDOWMENTS/LIFE PORTFOLIOS TO 01/10/2017 (REFER NOTES)

	PERFORMANCE PROFITS									SMOOTHED BONUS			STABLE FUND			CPI
	Equity %			Balanced %			Select %			%			%			
Period	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	%
1 Year	6.2	2.1	2.1	7.4	4.4	4.4	5.8	2.1	2.1	6.1	6.2	6.2	3.7	3.7	3.7	4.8
2 Years	3.1	3.4	4.0	5.0	5.0	5.3	3.2	2.9	3.3	6.5	8.3	7.0	3.7	3.6	3.6	5.3
3 Years	2.9	3.7	4.0	4.8	5.2	5.5	2.9	3.8	4.6	7.2	7.5	8.2	12.2	3.5	3.4	5.1
5 Years	6.1	7.2	10.7	6.6	7.3	9.4	5.5	6.4	9.0	8.9	9.2	10.5	3.2	3.1	2.8	5.6
8 Years	9.8	9.9	11.0	8.5	8.7	9.1	8.0	8.3	9.0	9.6	9.6	9.5	2.9	2.9	2.8	5.2
10 Years	9.4	9.2	6.6	8.3	8.2	6.6	8.1	7.9	6.4	9.4	9.3	8.9	3.0	3.1	3.5	6.0
15 Years	10.7	10.7	11.7	11.3	9.1	9.9	9.3	9.4	10.6	10.2	10.2	10.4	3.5	3.5	4.0	5.8
20 Years	10.8	11.0	10.3	9.3	9.4	9.1	-	-	-	10.1	10.1	9.9	4.0	4.0	5.0	6.2
25 Years	10.9	11.1	12.0	9.5	9.6	10.4	-	-	-	10.3	10.3	10.7	4.9	5.0	6.3	6.7
INTERIM RATES										8.00% p.a. (0.643% p.m.)			0.299% p.m.			

GUARANTEED CAPITAL FUND (CURRENT AFTER-TAX RATE)		4.70% p.a. (0.383% p.m.)
EQUIVALENT RETURN	at the tax rate of 18%	5.73% p.a. (0.466% p.m.)
	at the tax rate of 41%	7.97% p.a. (0.641% p.m.)

PORTFOLIO ASSET SPLIT

	RETIREMENT ANNUITIES						ENDOWMENTS/LIFE					
	PP Equity %	PP Balanced %	PP Select %	Smoothed Bonus %	WW Equity %	WW Balanced %	PP Equity %	PP Balanced %	PP Select %	Smoothed Bonus %	WW Equity %	WW Balanced %
Interest-bearing	0 (0)	26 (2)	16 (0)	25 (0)	0 (0)	27 (27)	0 (0)	26 (2)	16 (0)	25 (0)	0 (0)	27 (27)
Ordinary Shares	100 (26)	67 (31)	75 (29)	66 (24)	100 (86)	73 (59)	100 (26)	67 (31)	75 (29)	66 (24)	100 (86)	73 (59)
Property	0	6	9	7	0	0	0	6	9	7	0	0
Other	0	1	0	2	0	0	0	1	0	2	0	0

Figures in brackets — international portion of sector weighting

TOP EQUITY HOLDINGS (SA)

	NAME	% SPLIT	SECTOR
1.	Naspers Ltd	12.9	Media
2.	British American Tobacco	5.3	Consumer Goods
3.	Sasol	4.0	Oil & Gas
4.	Steinhoff International Holdings	3.8	Industrials
5.	Standard Bank	3.3	Banks
6.	Barclays Africa	3.2	Banks
7.	Old Mutual	3.0	Life Insurance
8.	MTN	2.8	Telecommunications
9.	FirstRand	2.4	Banks
10.	Remgro	2.4	Industrials

GLOBAL ECONOMIC OVERVIEW

September was a very good month for global equity markets. The US S&P 500 Index rose by 1.9% and closed the month at a new record. The German Dax fared even better, surging by 6.5%, almost fully reversing a cumulative similar-sized decline over the previous two months.

Good equity market performance came in spite of a number of developments that one would normally expect to cause some concerns among investors. These include ongoing concerns over geopolitics, as the tensions between the US and North Korea ratcheted up, warnings by several key central banks of policy normalization (either interest rate hikes or the start of balance sheet rundowns), and some signs of economic slowdown in China after the unexpectedly good second quarter growth outcome.

The fundamental reasons for the strong equity market performance are likely threefold. First is the growing confidence that the global economic recovery not only remains on track, but is spreading around the world. As a result, corporate profitability has remained generally healthy.

The second, almost perverse, reason for the good equity performance is that investors see central banks' willingness to push on with policy normalisation as a sign of policymakers' growing confidence that the global recovery is becoming self-sustaining, thus requiring less monetary support. Put differently, investors view policy normalisation as being for a good reason (that is, firming and spreading growth) and not for a bad reason (i.e. having to curb inflation pressures). Indeed, in recent months inflation surprises have been more on the downside than the upside, giving confidence that central banks are "not behind the curve'. In short, the perceived global macroeconomic "Goldilocks" environment (not too hot to cause inflation and not too cold to cause a recession), which we described in last month's commentary, has overridden pretty much all other potential concerns for investors over the past month.

As September drew to a close, the third reason for equity optimism appeared, namely renewed hope that the thus far postponed tax reform and fiscal stimulus in the US is back on the agenda. While the White House's fiscal plan still faces many obstacles and challenges, there is growing optimism that 2018 will indeed see some fiscal stimulus being implemented. This will lend further support to the US economy (and, by implication, the world), also supporting corporate profitability. While fiscal stimulus may eventually force the US Federal Reserve (Fed) to normalise policy faster than otherwise would have been the case, investors are, for now, happy to focus on the boost to the economy and profits.

While markets have been cheering the good global environment, and correctly so, one should never lose sight of the inevitable risks that still exist. The most important is that investors may be too complacent about the extent of central bank policy tightening. Despite a clear signal from the Fed of their intention to raise interest rates at the pace indicated at the September policy meeting (that being a hike in December and three more next year), markets are generally more complacent, seemingly thinking the Fed will do less. The same goes for the start of the rundown of the Fed's US$4.5 trillion balance sheet. Common market perception is that it has been so well signalled by the Fed that it is largely in asset prices and will therefore not have much impact. The next few months will tell whether investors have simply become too complacent and markets have priced in too much good news.

In the meantime, we remain positive on the outlook for the world economy, as we have been for some time, with no serious headwind in sight that could derail this outlook.

GLOBAL MARKET PERFORMANCES IN RAND TERMS

	LAST MONTH (%)	YEAR TO DATE (%)	1 YEAR (% P.A.)	3 YEARS (% P.A.)	5 YEARS (% P.A.)	8 YEARS (% P.A.)	10 YEARS (% P.A.)
MSCI World	6.3	15.1	16.7	14.9	23.2	18.5	12.1
JP Morgan	2.7	4.4	-4.8	7.4	10.1	9.3	10.4
S&P 500	6.0	12.8	16.5	17.6	26.0	22.3	14.8
FTSE 100	7.4	14.3	12.8	7.3	16.0	14.1	7.9
Nikkei Index	5.2	9.0	9.3	13.6	21.0	14.0	9.3
Rand/Dollar	3.9	-1.3	-1.8	6.1	10.4	7.5	6.9

WORLDWIDE FUNDS: PERFORMANCE IN RAND TERMS – REFER NOTES

	WW EQUITY %						WW BALANCED %					
	Retirement Annuities			Endowments/Life			Retirement Annuities			Endowments/Life		
Period	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.	M.P.	A.P.	S.P.
1 Year	24.2	16.2	16.2	20.6	14.0	14.0	19.3	10.4	10.4	16.0	8.9	8.9
2 Years	12.8	13.8	12.8	10.9	11.9	11.0	8.6	9.5	9.1	6.8	7.9	7.5
3 Years	12.2	12.7	11.7	10.8	11.3	10.7	9.7	10.2	10.8	8.1	8.8	9.6
5 Years	14.0	15.4	18.6	12.9	14.1	17.6	12.1	13.2	16.3	10.8	11.9	15.2
8 Years	15.7	16.0	14.5	14.8	15.1	13.8	13.8	14.0	12.9	12.9	13.1	12.3
10 Years	13.6	13.1	7.4	12.8	12.3	6.7	12.2	11.9	8.1	11.4	11.1	7.4
15 Years	10.9	10.6	8.2	10.0	9.7	7.0	10.6	10.2	7.8	9.7	9.4	6.8

GEOGRAPHICAL SPREAD

	EQUITY PORTION %			BOND PORTION %		
	Fund	MSCI	Difference	Fund	Benchmark[7]	Difference
United States	41.9	52.1	-10.1	33.4	38.6	-5.2
Japan	3.9	7.6	-3.7	4.2	16.8	-12.6
Europe ex UK	19.4	16.1	3.3	33.6	28.6	5.0
United Kingdom	6.6	5.9	0.7	8.8	5.5	3.3
SE Asia & Canada	10.3	12.0	-1.7	14.8	8.5	6.4
South Africa	14.5	0.0	14.5	0.0	0.2	-0.2
Other	3.4	6.3	-2.8	5.2	1.8	3.4
Total	**100.0**	**100.0**	**0.0**	**100.0**	**100.0**	**0.0**

EQUITY SECTOR SPREAD

	Fund	MSCI	US	JAPAN	UK	Europe ex UK
Cash	2.9	0.0	1.4	0.1	0.2	0.7
Consumer Discretionary	8.4	11.9	4.1	0.4	0.7	1.9
Consumer Staples	6.2	8.8	3.0	0.3	0.5	1.4
Energy	4.3	6.4	2.1	0.2	0.3	1.0
Financials	17.2	18.7	8.4	0.8	1.3	3.9
Healthcare	10.9	11.2	5.3	0.5	0.8	2.5
Industrials	11.1	10.8	5.4	0.5	0.9	2.5
Information Technology	14.4	17.6	7.0	0.7	1.1	3.3
Materials	4.6	5.3	2.3	0.2	0.4	1.0
Other	0.9	0.0	0.4	0.0	0.1	0.2
Telecoms Services	1.6	3.2	0.8	0.1	0.1	0.4
Utilities	1.5	3.1	0.7	0.1	0.1	0.3
SA Rand Hedge	14.5	0.0	0.0	0.0	0.0	0.0

TOP EQUITY HOLDINGS (GLOBAL)

NAME		SECTOR
1.	JPMorgan Chase & Co	Financials
2.	Oracle Corporation	Information Technology
3.	Fiat Chrysler Automobiles	Consumer Discretionary
4.	Moody S Corporation	Financials
5.	Alphabet Inc	Information Technology
6.	Apple Inc	Information Technology
7.	Bank of America Corporation	Financials
8.	DS Smith Plc	Industrials
9.	Wells Fargo & Co	Financials
10.	Keyence Corporation	Information Technology

NOTES

1. The performance figures in the tables represent the returns earned on premiums allocated. The returns on premiums actually paid will be lower than this because they take the policy specific charges into account.

2. All returns are quoted net of investment fund charges and tax.

3. The Smoothed Bonus declaration is made up of a vesting bonus and a claim bonus. The vesting bonus portion of the total bonus cannot be removed on death or maturity of the policy. The claim bonus portion is not guaranteed and could be adjusted should investment conditions dictate.

4. M.P. = monthly premium, A.P. = annual premium, S.P. = single premium.

5. The Flexi range of products was launched on 1 September 1984. Returns for the periods starting before this date apply to policies available before the introduction of the Flexi range of products.

6. The Property Portfolio and the OMD Top 40 Index Fund returns are available at any time.

7. The MSCI World Index is the benchmark for the Worldwide Equity portion. The benchmark figures for the Worldwide Bond portion consist of 70% JP Morgan Bond Index and 30% Barclays Capital Global Bond Index.

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